

COMMONWEALTH OF KENTUCKY  
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

AN ADJUSTMENT OF RATES OF DELTA )  
NATURAL GAS COMPANY, INC. ) CASE NO. 9059

O R D E R

On January 10, 1985, Delta Natural Gas Company, Inc., ("Delta") filed a motion for rehearing of certain issues decided in the Commission's Order of December 21, 1984. On January 30, 1985, the Commission entered an Order granting rehearing on the issues of Depreciation Expense, recovery of the expense of an Organizational and Compensation Study, and Gas Plant Acquisition Adjustment. The Order granted immediate rate relief of \$31,944 on two of the issues and deferred a decision on the Plant Acquisition Adjustment issue pending further investigatory procedures.

Delta submitted prefiled testimony on March 1, 1985, and a hearing was conducted on April 30, 1985, on the Plant Acquisition Adjustment issue. Responses to requests for information at the hearing were submitted. Delta submitted a rehearing memorandum on May 24, 1985.

The gas plant acquisition adjustment in this case stems from the purchase by Delta in October 1977 of Gas Service Company, Inc. ("Gas Service Co."). Delta acquired Gas Service Co. from Graham-Michaelis Drilling Co. ("Graham-Michaelis") through the

purchase of all of the capital stock at net book value. At the time of the purchase, Gas Service Co. had a gas plant acquisition adjustment on its books in the amount of \$411,160 with an unamortized balance of \$255,635. The plant acquisition adjustment on the books of Gas Service Co. was initially recorded on the books of Williamsburg Gas Company, Knox Gas, Inc., Pineville Gas Company, and Gas Service Company, which were consolidated into Gas Service Co. in 1974. Apparently, these acquisition adjustments were generated when Graham-Michaelis acquired these local distribution companies in South Central Kentucky. Since the acquisition by Delta of Gas Service Co. was a stock transaction, the plant acquisition adjustment was not affected as a result of that purchase. Gas Service Co. was initially operated as a subsidiary of Delta until 1979, when Delta consolidated these operations.

In Delta's first rate case after its acquisition of Gas Service Co., the plant acquisition adjustment was not an issue of contention. None of the parties to the proceedings contested the inclusion of the adjustment in rate base or the amortization expense. The acquisition adjustment was included in the revenue requirements determination. In subsequent cases, 8256 and 8528,<sup>1</sup> the Commission excluded the adjustment from rate base and the annual amortization was not allowed for rate-making purposes. The decision of the Commission in those cases was in keeping with the

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<sup>1</sup> Case No. 8256: Notice of Adjustment of Rates of Delta Natural Gas Company, Inc.

Case No. 8528: Notice of Adjustment of Rates of Delta Natural Gas Company, Inc.

standard treatment accorded plant acquisition adjustments in other utility cases. The treatment of the plant acquisition adjustment is now an issue before the Franklin Circuit Court on Delta's appeal of the Orders in Delta's previous two rate cases.

The treatment of the gas plant acquisition adjustment in this case does not have a material impact on the rates of Delta. The Commission does, however, feel that the issue is of sufficient importance to merit more than cursory consideration. This Commission has concluded that plant acquisition adjustments should not be denied as a matter of rigid rate-making policy but that each instance should be evaluated on its own merits and, if it is demonstrated that the acquisition at a cost above book value is in the public interest, the utility should be allowed to recover its investment. The Commission maintains its position that the net original cost of plant devoted to utility use is the fair value for rate-making purposes, unless the utility can prove, with conclusive evidence, that the overall operations and financial condition of the utility have benefited from acquisitions at prices in excess of net book value. The burden of proof is upon the utility to justify its investment at the price in excess of net original cost based on economic and quality of service criteria. In order to meet this burden of proof, evidence must be submitted that shows that the purchase price was established upon arms-length negotiations, the initial investment plus the cost of restoring the facilities to required standards will not adversely impact the overall costs and rates of the existing and new customers, operational economies can be achieved through the

acquisition, the purchase price of utility and non-utility property can be clearly identified, and the purchase will result in overall benefits in the financial and service aspects of the utility's operations.

At the time Delta purchased Gas Service Co., the service was substandard. Poorly constructed and inadequately maintained gas lines had severe leakage problems and service was unreliable. Delta had been encouraged by the Commission to acquire Gas Service Co. and, as a part of its application to acquire Gas Service Co., Delta made a commitment to invest heavily in upgrading the facilities to insure a reliable gas supply for its consumers. Delta contended that, while it was considering the purchase of Gas Service Co., in a meeting with Commission staff it was led to believe that the plant acquisition adjustment could be recovered through rates.

The majority position of the Commission in the original Order in this proceeding was that Delta had failed to provide conclusive evidence that the plant acquisition adjustment was justified. Chairman Richard Heman dissented from the majority opinion and stated that the acquisition adjustment should be allowed. The Commission granted a rehearing to allow Delta the opportunity to file additional proof on the issue.

The primary evidence in support of the acquisition adjustment presented by Delta is the improved quality of service. The Commission cannot disagree with Delta's contention that safety and reliability of gas service in the acquired area has improved substantially. Delta has done a commendable job in renovating and

operating the acquired system. In this instance, the Commission is of the opinion that Delta has proven that the overall operations and financial condition of the utility have benefited as a result of its acquisition and that it should be allowed a return on its full investment, including the plant acquisition adjustment. Therefore, the Commission will include the plant acquisition adjustment in rate base and allow the amortization of the plant acquisition adjustment in determining the cost of service and revenue requirements herein.

IT IS THEREFORE ORDERED that the allowed revenues be increased by \$22,378 annually, based upon the findings herein.

IT IS FURTHER ORDERED that the rates and charges in Appendix A shall, to the extent of their differences, supersede the rates authorized in the Commission's Orders of January 30, 1985, and December 21, 1984, and are hereby approved for service rendered by Delta on and after the date of this Order.

IT IS FURTHER ORDERED that all other aspects not specifically mentioned herein of the Commission's Order of December 21, 1984, are hereby affirmed.

Done at Frankfort, Kentucky, this 11th day of September, 1985.

PUBLIC SERVICE COMMISSION

Richard L. Herman  
Chairman

Robert L. L.  
Vice Chairman

James H. Williams  
Commissioner

ATTEST:

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Secretary

AMENDED APPENDIX A

APPENDIX TO AN ORDER OF THE KENTUCKY PUBLIC SERVICE  
COMMISSION IN CASE NO. 9059 DATED 9/11/85.

The following rates and charges are prescribed for the customers served by Delta Natural Gas Company, Inc. All other rates and charges not specifically mentioned herein shall remain the same as those in effect under authority of this Commission prior to the date of this Order.

The following rates and charges have incorporated all changes through PGA Case No. 9059-C.

RATE SCHEDULES

AVAILABILITY

Available for general use by residential, commercial, and industrial customers who purchase their entire natural gas requirements from Delta.

RATES

	<u>Base Rate</u>	<u>Gas Cost Recovery Rate</u>	<u>Total Rate</u>
	plus		equals
General Service			
Monthly Customer Charge			\$3.90
1 - 1,000 Mcf	\$1.9796	\$4.0843	\$6.0639 per Mcf
1,001 - 5,000 Mcf	1.8311	4.0843	5.9154 per Mcf
5,001 - 10,000 Mcf	1.5311	4.0843	5.6154 per Mcf
Over 10,000 Mcf	1.2311	4.0843	5.3154 per Mcf
Interruptible (2)			
1 - 1,000 Mcf	\$1.7296	\$4.0843	\$5.8139 per Mcf
1,001 - 5,000 Mcf	1.5811	4.0843	5.6654 per Mcf
5,001 - 10,000 Mcf	1.2811	4.0843	5.3654 per Mcf
Over 10,000 Mcf	0.9811	4.0843	5.0654 per Mcf